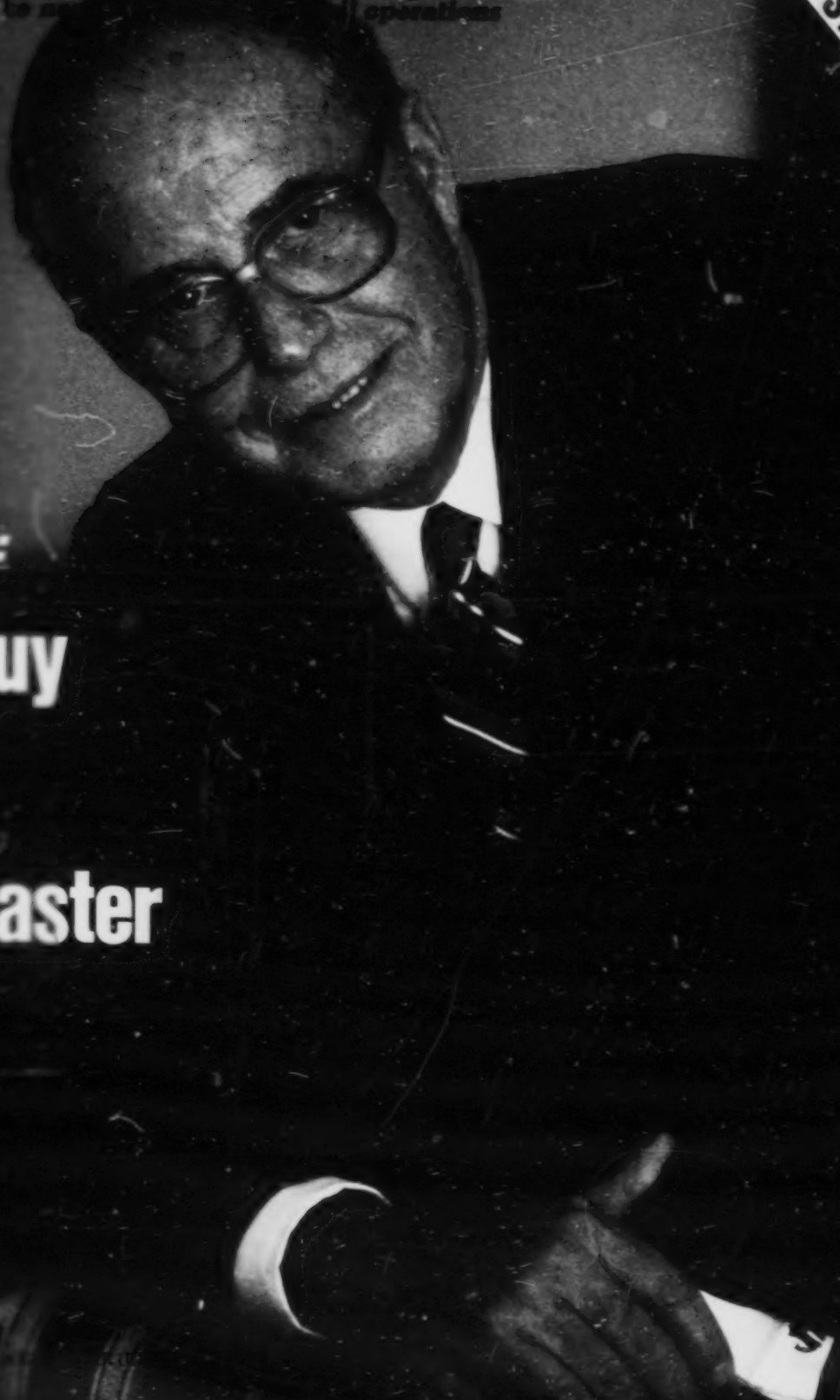
Chain Store Age
EXECUTIVE
With Shopping Center Age
January 1985

NRMA CONVENTION
1984 TAX ACT STUDY



ADG's Joseph Johnson:

Nice guy but stern taskmaster

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Basic similarities of the family rack store and the one-price outlet account for their mutual success, according to Pic 'N Pay president Edward Karp.

"They're both self-service; they have the same price points, and they offer value because of the low expense factor and the volume [buying]," he says. Further, both Barett and Pic 'N Pay stores operate in 2,500-3,500 sq. ft., high-traffic locations, making the two businesses a good match. As might be expected, some Barett stores are converted Pic 'N Pay units.

What puzzles many industry experts--and no doubt concerns the box-store operators—is whether the rack chains are squeezing more business out of their traditional market segment or taking customers away from higher-price outlets. And, they wonder, how much longer can the self-service sector accelerate before it stalls?

To some, the headlong expansion of concepts like the $13.88 store is an inexplicable, possibly ill-fated phenomenon. "I don't know where the business is coming from," First Boston's Gilliam says, adding that she doesn't think there is any trading down to speak of. "To me, it looks like something that is going to explode and die."

Mangione of the VFRA suggests that the rack sector might have created new business, accounting for the lion's share of domestic footwear consumption growth in recent years. (Commerce Department estimates show that per capita spending on footwear rose to $101.60 in 1983 from $87.89 in 1982, with price increases in the interim described as "minimal.")

Of course, not all the big rack operations have been stellar performers. Analysts note the unsteady course of Morse Shoe's giant Fayva chain, which was trimmed by a net 139 units in 1983. Morse reported flat margins in the first half of 1984, due in part to promotional activity in the Fayva division. Some sources contend that Fayva's marketing aimed too high.

"They went after a customer above where we are. They've seen themselves competing very head on with Kinney, Edison Bros. and the department store business," Stutzman says. "That's a tough bunch of people if you're going to hit heads with them."

With its average shoe selling at $14, Volume tries to squeeze in above the discounters and below the box stores. Its target customer is female, under 35 years of age, married and with children living at home, backed by a household income of $20,000 or less and responsible for 80% of her family's footwear purchases. Stutzman promises Volume will remain faithful to that consumer, even though research is under way to check management's assumption that the customer base is broadening upward.

Nevertheless, Stutzman is convinced that Volume is raiding other shoe retailers for business. "We've got to be getting it out of some of the mass merchandisers, out of the discounters, out of the conventional box stores—it's got to be coming from there. Not all of it but some of it. People who are shopping today in self-service stores weren't shopping there five or 10 years ago," he says.

Many in the shoe business share Stutzman's view that the average shopper is no longer averse to buying shoes from a rack.

"The consumer today would rather not have anyone wait on him or her than someone who is discourteous and unknowledgeable," argues William Boettge, president of the National Shoe Retailers Association.

But Cameron I. Anderson, president of Kinney, for one, doubts whether today's booming rack chains pose a long-term threat to his business. "There's no question that they've had growth. But I'm not convinced that they've proved themselves under continuous competitive fire," he says. Historically, he points out, the low-price business has been volatile and littered with casualties. Some of them, such as HRT Industries' Shoe Stop stores, were gobbled up by Volume.

"I do think the market under $15 is a market unto itself," he says, conceding that a good rack store can temporarily impact a Kinney store on certain price-lines.

Stutzman agrees that a Payless store won't truly salvage a nearby Kinney store. "Really impact? No. Share some of their customers with them? Yes. We'll share some of their customers." ■

—Gary Vineberg

RESEARCH STUDY

Survey: 35% don't comply with 1984 Tax Reform Act

Without much fanfare, the Tax Reform Act of 1984—which includes a section invalidating retailing's method of granting different discounts to executives than to nonexecutives—went into effect on Jan. 1.

And, according to a survey by *Chain Store Age Executive* in conjunction with Arthur Young, an international accounting and consulting firm, 35% of retail chains aren't in compliance with the act. The department store segment appears to be the retail group that is most affected by the act as it relates to employee discount policy. At the time of the survey, 4 out of 5 department stores reported a situation that wasn't currently in compliance with the statutes of the new law, compared with 37% of discount stores, 27% of specialty stores and 23% of home centers.

Moreover, the survey discloses, 31% of the retailers haven't any immediate plans to make the necessary changes to be in compliance even though the Internal Revenue Service

Discount offered to executives and nonexecutives*
(among those differentiating between the two)

Per cent discount offered	Nonexecs	Execs	Dept. store nonexecs	Dept. store execs
5%-10%	11%	—	4%	—
11%-15%	11	—	9	—
16%-20%	47	14%	61	9%
21%-25%	3	19	4	22
26%-30%	6	8	—	9
31%-35%	—	6	—	9
36%-40%	—	8	—	4
41%-45%	—	—	—	—
46%-50%	—	3	—	—
10%-20%	11	—	13	—
20%-40%	—	8	—	13
20% + 20%	—	11	—	17
Other	11	22	9	17
Mean	(16.6)	(27.3)	(17)	(26.3)

*Individual percentages may not equal 100% due to rounding
Source: *Chain Store Age Executive* research

Respondents' perception about company's compliance situation*

Comment	Total	Dept.	Discount	Drug	Home center	Specialty
No change needed	84%	23%	93%	93%	73%	73%
—Policy seems O.K.	57	20	40	87	70	67
—Policy not O.K.	7	3	13	7	3	7
Already changed policy	14	43	10	—	10	7
No plans to change	10	33	37	7	10	17
—Policy seems O.K.	3	—	23	7	3	7
—Policy not O.K.	11	23	13	—	7	10
Insufficient knowledge	4	10	—	—	7	3

*Individual percentages may not equal 100% or net due to rounding
Source: *Chain Store Age Executive* research

set Jan. 1 as the date of the legislation's effectiveness. (Retailers have said the IRS plans to issue more specific regulations relating to retailers later this month even though the law is already in effect.)

Says one specialty store chain owner: "I'm satisfied with the way things are now. I've been in business 53 years and see no reason to change. I didn't even know about the new law."

In fact, 33% of the retailers contacted say they never heard of the act. Only 10% of the retail executives who responded to the survey say they are "very familiar" with the section relating to employee discounts, and 55% say they are "somewhat familiar." This seems to be an indictment of someone: either retailers aren't keeping abreast of changing legislation, or the IRS isn't making sure those affected have been informed. Still, 14% of the chains say they have already changed or planned to change by the Jan. 1 deadline in order to comply with the new law.

Among department store respondents, 23% say they are "very familiar," 70% say they are "somewhat familiar" and 7% weren't familiar at all with the section. Specialty store executives were low on the totem pole with 73% saying they never heard of the employee discount section, while 43% of discount store executives, 20% of drug chains and 23% of home center executives also say they never heard of it.

Of the chains that plan to make changes in their discount policy, 52% plan to offer a single per cent discount to everyone. Other policy changes volunteered by respondents include:

- 14% say no discount will exceed the overall gross margin percentage.
- 14% say alternate benefits are being offered instead of discounts.
- 10% plan to issue withholding statements to employees whose discounts are not in compliance.
- 5% say all divisions will offer the same discount.
- 5% plan to make all the necessary changes.
- 29% say that plans haven't been finalized.

The act, passed by Congress in mid-1984, is an all-encompassing piece of legislation that affects many aspects of taxation—including tax shelters, family wealth transactions and excise taxes. The legislation affecting retailing is but one minor part of the act and zeros in specifically on retailers who grant discounts as an employment benefit.

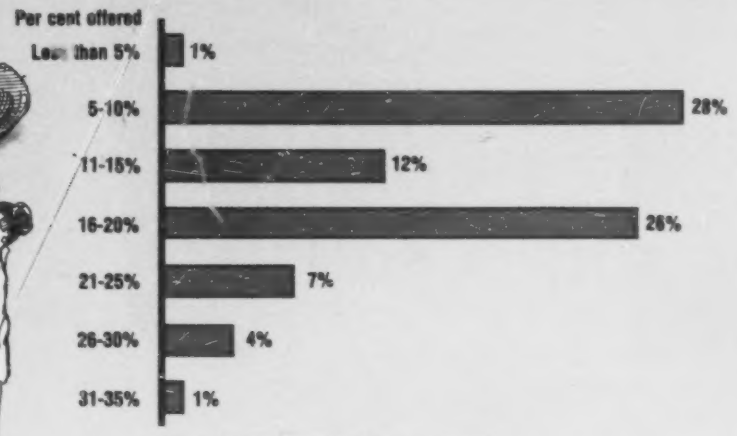
It was included in the legislation after some leading retail chains asked the IRS to exempt employee discount from taxable income. The IRS, in turn, said it would consider that request if retailers would stop their practice of giving different discount percentages to executives than are given to nonexecutives. The IRS added some qualifications:

- Discounts are given to all employees on an equal basis.
- Discounts do not exceed the employer's gross margin percentage for goods sold, or—in the case of services—20% of the retail value of the service.
- Discounts are offered only in the employer's line of business.

The major violation situation, according to the survey, is two or more levels of discounts to employees, differentiating between executives and nonexecutives. The largest practitioner of this violation is the department store category, with 96% saying they grant multiple discounts depending on rank or length of service.

In addition, 35% of all respondents say the discounts they offer are greater than the overall gross margin percentage, while 25% say that the discount depends on the employee's length of service.

Of the total, 40% weren't currently



in compliance in 1984, but had plans to be (in compliance) by Jan. 1, 1985. Although 19% say they are in compliance, some of their answers to other questions in the survey indicate they are not.

Major reasons cited in the survey for not being in compliance with the new law include:

- Waiting to hear from corporate headquarters.
- Waiting for IRS regulations.
- Ignorance of the legislation (10% say they don't have enough information to comment).

The survey discloses that department stores may be in the biggest trouble with the IRS if it suddenly cracks down on retailing.

A whopping 80% of department stores aren't currently in compliance with the statutes of the new law, compared with 37% of discounters, 25% of specialty stores, 23% of home centers and 7% of drug chains.

A check of supermarket chains discloses that few offer discounters to employees, especially different discounts to executives and nonexecutives.

Of the total respondents, 24% say they offer different employee discounts to executives and nonexecutives. The department store chains were the highest, with 77% distinguishing between executives and nonexecutives, followed by 23% of discounters, 13% of specialty stores and 3% each for drug stores and home centers.

Overall, retailers offer their nonexecutives an average discount of 16.6%, while executives average 27.3%. Twelve respondents say that owners, store principals or corporate officers get even higher discounts than lower level executives, the highest being between 46% and 50% in the specialty store category.

One specialty store executive says about discounts: "No executives except myself, and I'm the owner." The survey shows that 33% of the chains have additional employee rank categories beyond that of executive and nonexecutive.

Of the total, 12% of the respondents allow some employee discounts larger than the overall gross margin percentage. This is most prevalent among department stores (23%) and discounters (20%).

The survey shows that 71% of the overall chains say they offer the same discounts to everyone from the ceo down to the stockboys. In this category, 28% say they offer discounts ranging between 5% and 10%, 12% say the discounts are between 11% and 15% and 26% say the range is between 16% and 20%.

In the single discount category, department stores have an average employee discount of 19.5%, followed by specialty stores (19.4%), drug stores (12.8%), home centers (12.4%) and discounters (12.2%).

A number of chains offer discounts based on length of time employees are with the company. The average discount per cent is: 16.2% for less than five years, 24.7% for a minimum of 10 years, 26.3% for a minimum of 20 years and 27.3% for employees who have worked 25 years or more with a chain. ■

Level of familiarity*

Degree	Total	Dept.	Discount	Drug	Home center	Specialty
Very familiar	11%	23%	7%	10%	17%	—
—Somewhat familiar	55	70	50	70	60	27%
—Not at all familiar	33	7	43	20	23	73

*Individual percentages may not equal 100% due to rounding
Source: *Chain Store Age Executive* research

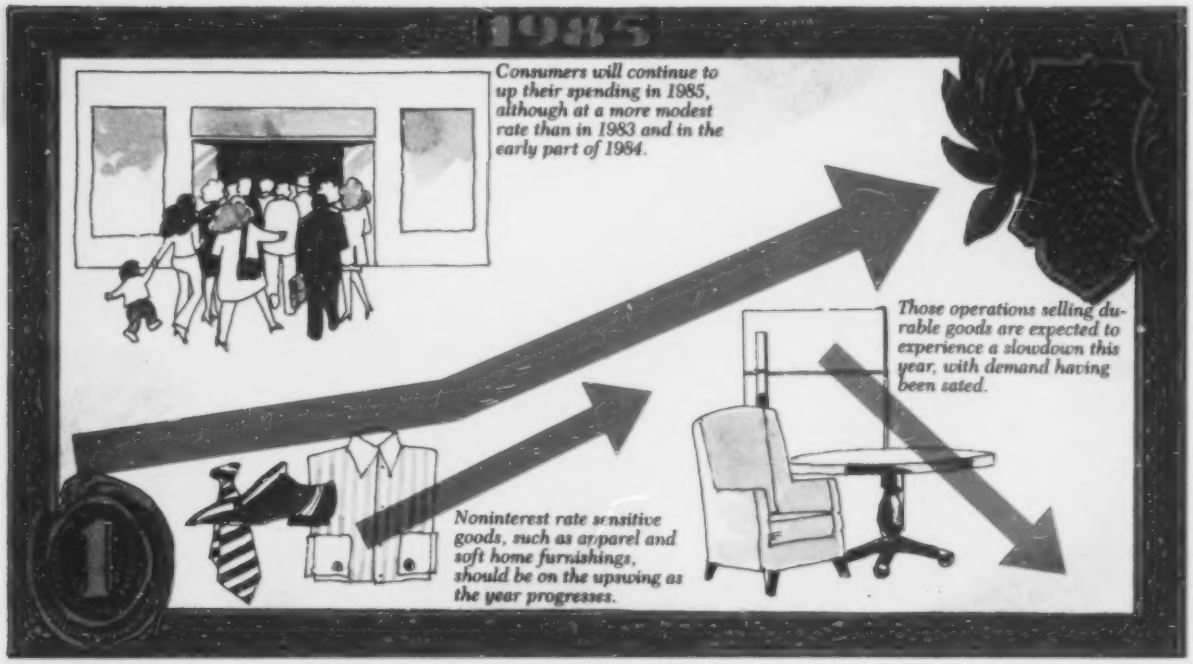
How survey was conducted

A total of 150 interviews were conducted among retail executives located throughout the country, consisting of 30 each from the department store, discount store, drug store, home center and specialty store categories.

Over half (55%) of the executives participating in the survey were chief financial officers. Other titles included: ceo (12%), controller (9%), treasurer (8%), vp-finance (7%) and general counsel (1%).

The average chain participating in the survey has 69 units and reported an annual dollar volume of $168.8 million in its last fiscal year. Of these department stores have an average of 15.8 units and a volume of $247.1 million; home centers have an average of 129.8 units and volume of $205.5 million; discount chains have an average of 38.2 units and $186.5 million volume; drug chains have an average of 133.4 units and $183 million volume, and specialty chains have an average of 26.9 units and $17 million volume.

Taking a conservative stance


1985
Consumers will continue to up their spending in 1985, although at a more modest rate than in 1983 and in the early part of 1984.
Those operations selling durable goods are expected to experience a slowdown this year, with demand having been sated.
Noninterest rate sensitive goods, such as apparel and soft home furnishings, should be on the upswing as the year progresses.

Retailers see retail sales growing at a more modest rate this year, reflecting the overall slowdown in the recovery

Blaming unrealized expectations for the high degree of promotional activity that's been taking place in the industry with somewhat depressing results, it is no wonder that most retailers are adopting a conservative outlook for the upcoming fiscal year. Their premise is that as goes the general economy, so go retail sales.

For example, predicting that growth in the gross national product may fall to as little as 1% during the first and second quarters of 1985, Maurice Segall, president and ceo, Zayre Corp., warns that "Retailers had better be lean and mean going into the first quarter and through the first half." In anticipation, he reports that Zayre has already set up a very flexible inventory open-to-buy program.

Likewise, Edward Finkelstein, chairman and ceo of R. H. Macy, says that "We've planned on a rather sluggish economy" for the early part of this year. Macy's buying programs are being adjusted accordingly.

However, not everyone is quite so pessimistic.

"I'm not one of those gloom-and-doom people," says Herbert Fisher, chairman of Jamesway. "I don't expect a banner year, but I don't think we'll do any worse in 1985 than we did in 1984." Specifically, he is projecting a 17% sales increase in fiscal 1985 with new stores contributing 10% and existing stores accounting for the balance.

Both points of view are likely to be debated by general merchandise retailers when they meet this month at the annual convention of the National Retail Merchants Association, the industry's largest trade group *(see accompanying story)*.

Much of the debate is likely to focus on just how much a general slowing down of the economy will, in fact, impact consumer spending.

At J. C. Penney, Rosalind Wells, manager of corporate economics, does not see a close correlation.

"We don't think perceptions of a slowdown in the economy will hurt retail sales," she says. "Consumers are still in a strong financial position and we expect consumer spending to pick up further this year. There is no reason to expect anything else." Her forecast calls for a consumer spending rise of 3.5% on top of 1984's 5.5% gain.

A major impetus is the fact that "Although unemployment is not dropping (projected to remain at approximately 7.5%) and wages and salaries are not increasing as rapidly as they had, inflation is lower so real disposable income is up," she points out.

Confirming this trend, Sandra Shaber, an economist with Chase Econometrics is forecasting an increase of 3.4% in real disposable income for this year, on top of the estimated rise that took place last year. She places the inflation rate at only 3.4%, approximately the same level as in 1984.

As a result of such positive factors, Wells sees sales of general merchandise, apparel and furniture (GAF) increasing by 7.5%. Based on her forecast of 3% GAF price inflation, this would translate to real gains of approximately 4.5%.

The gains are strong enough in themselves. They are even more significant, though, since they follow the 1984 increases which indicate the strongest sales performance in these categories since 1971, points out Wells. Last year GAF industry sales are estimated to have risen 9.5% in real terms, taking into account general merchandise inflation which is placed by Wells at approximately 2%.

Yet, the improvement in sales per-

Maurice Segall, president and ceo, Zayre

"Retailers had better be lean and mean going into the first quarter and through the first half"

Herbert Fisher, chairman, Jamesway

"I don't expect a banner year, but I don't think we'll do any worse in 1985 than we did in 1984"

Philip Hawley, chairman and ceo, CHH

"While we expect a slowdown in the sales growth rate, we expect very strong profit growth"

formance may not be experienced by all retail categories, according to Wells. "In 1985, noninterest rate sensitive goods, such as apparel and soft home furnishings, should do better than the housing related, big ticket durables," she says.

James Newton, director of economic research for Management Horizons, agrees that "One type of retail institution that we view as likely to experience a considerable slowdown is those operations selling durable goods." These include furniture stores, consumer electronics stores, appliance stores and even automobile showrooms. In 1983 and 1984 these areas experienced extremely high growth. Now they are slowing up as demand has been sated." Management Horizons' forecast calls for durable goods sales growth to slow to 3% this year, from 1984's 12.8%.

However, he adds, "One area we see continuing to do relatively well is apparel. But even there we're looking for a slowdown." According to his estimates, while purchases of these goods rose at a more modest rate of only 4.9% in 1984, they are seen as increasing an additional 2.9% in the current year.

The net result is that "We see continuing improvement in retail sales, but not at the same rates as for most of this year," he says. "While retail sales growth was in excess of 7% in 1984, we see it being approximately 3% this year."

Howard Hassler, senior vp and cfo of Allied Stores, says, "We expect that this will be a fair year. But we don't anticipate as much of an upturn as we experienced in 1983 and earlier in 1984 when sales were very strong. We expect reasonable increases but we are unsure what impact all the proposed tax changes may have."

The new Federal tax proposals also pose a big question mark to the Caldor discount store chain. "We're planning for the spring to be as good as last year, or maybe even better," says Harold Karun, executive vp-finance and administration. But, because of the uncertainty over taxation legislation, he refuses to speculate on what will happen during the second half of the year.

Other retailers, though, appear relatively confident that by the third and fourth quarters, traditionally the most important retail selling seasons, sales will clearly be on the upswing. For example, "I think the second half, particularly the fourth quarter, will see us in a more healthy growth situation," says Segall.

As for what the final outcome will be, Philip Hawley, chairman and ceo of Carter Hawley Hale, believes that for the year in total "Industrywide we

NRMA show planned for Jan. 13-16

"Retailing '85: Focus on the Future" is the theme of the 74th annual convention and National Retailers Business & Equipment Exposition, sponsored by National Retail Merchants Association, Jan. 13 through Jan. 16, in the New York Hilton and Sheraton Centre hotels.

From the opening session of the convention on Monday, Jan. 14, which will feature talks on economic and retail projections for 1985, the convention will look at retailing through 1990, evolving concepts in retailing, the inside information on MBAs in retailing, protectionism vs. open-door trading, national brands vs. private labels, and a multitude of meetings on merchandising and store planning, as well as such specialized subjects as security.

Starting at noon on Sunday, Jan. 13, and running through 3 p.m. on Wednesday, Jan. 16, the Business & Equipment Exposition will feature exhibits by manufacturers and resources involved in electronic cash registers and point-of-sale systems, data processing, management information systems, communications and telecommunications, merchandise marking and coding, business machines and equipment, security and loss prevention, financing and banking transactions, store planning, design and construction, visual merchandising, displays, fixtures, lighting and signmaking, merchandise handling, marketing, sales promotion and packaging.

Selected economic statistics*
(year-to-year changes)

	1980	1981	1982	1983	1984E	1985E
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Consumer spending:						
Durables	− 6.6	+ 2.5	−0.3	+12.1	+13.0	+ 3.1
Nondurables	+ 0.7	+ 1.5	+0.6	+ 3.7	+ 5.8	+ 3.7
Services	+ 2.7	+ 3.3	+2.9	+ 2.7	+ 3.3	+ 2.8
Housing starts (thousands, annual rate)	1,300	1,096	1,059	1,704	1,817	1,550
Prices						
Consumer Price Index	13.5%	10.3%	6.2%	3.2%	4.1%	4.8%
General merchandise	6.3	4.7	2.8	2.7	3.5	4.2
Unemployment rate (% of labor force)	7.2	7.6	9.7	9.6	7.5	7.2

*In real dollars
Source: Morgan Stanley

will see more moderate sales increases." For CHH specifically, he says that "While we expect a slowdown in the sales growth rate, from excellent to very good, we expect very strong profit growth." This growth "is a payback from our restructuring program and from the merchandising strategy we instituted early in 1983 and which was already evident in the third and fourth quarters of this past fiscal year."

The biggest question mark, though, remains interest rates. "I think we are going to see upward pressure on interest rates, all caused by the twin deficits—the Federal deficit and the trade deficit," says Shaber. "If interest rates increase, and I believe we are right in forecasting that they will, I think this may undermine consumers' confidence in the economy."

She adds, "For several decades interest rates played little role in consumer spending, but in the last couple of years they have become very important. There definitely has been a relationship in terms of nominal interest rates and consumer spending. People are sensitive to interest rates as never before."

Yet, most retailers are echoing the sentiments of Joseph Johnson, chairman and ceo, Associated Dry Goods, who says, "Even though the economy generally seems to be slipping somewhat in the last few months, according to everything I read in the papers, I would still forecast 1985 to be a good sales year for retailers."

Specifically, he says, "I would still expect we're going to have an increase in department stores, for competitors as well as ourselves, somewhere around 7.5% to 8%, and doing better in discount stores."

If retailers can achieve such gains in the third year of an economic recovery and with most other economic indicators slowing sharply, chances are they will still be content. ■

Consumers still opening wallets, keeping sales strong

Retailers have varying opinions on how their businesses will fare during 1985, dependent somewhat on whether they are selling impulse goods or basic "necessities."

In general, specialty store retailers have diminished expectations for the United States economy in 1985. They see the unresolved issues of Federal deficit and tax reform proposals dampening consumer enthusiasm at least through the year's halfway point.

"We think 1985 will be a tough year economically in general," offers Harry E. Rich, senior vp of St. Louis-based Brown Group. Rich says consumers will probably be tight-fisted for the first six to eight months, suppressing retail sales. The company also expects to be hurt somewhat by a national oversupply of shoes.

Richard P. Hamilton, chairman and ceo of Hartmarx, is considerably more hopeful. "If things should slow down, we think we'll perform above the average," he says.

"When we had the last recession [1981-82], we sailed right through it beautifully," Hamilton says. The company's core customer—the 35-55 year old business/professional man—is not usually affected by slight economic downturns, he observes.

However, there will be "a little trepidation" among consumers for the first six months of 1985, warns Bert Briskin, executive vp of Brooks Fashion Stores.

The 35- 55-year-old business/professional man is not usually affected by slight economic downturns

Briskin cited the pending Federal tax reform proposal, among other worries, as a source of consumer uncertainty. "They'll play their spending a little closer to the vest until things settle down."

Briskin still feels Brooks will post sales increases in the first half, and better increases in the second half, but qualifies his projection: "It won't be as strong as it was in the past two years. There'll be a slowing down."

In contrast, as Martin Grass, senior vp-planning and development of Rite Aid, says, "In the drug store business we are little bit lucky because we are selling necessity. Our own business hasn't skipped a beat through the recession."

He adds, "This year our company is looking for another record year of sales and profits."

As for the economy at large, "I think there is not going to be much difference in the economy this year from where it was last year. Basically I believe we are going to stay about where we are now at least for another year."

Peter Rhodes, cfo, Fay's Drug Stores, who agrees with Glass, adds that while last year the economic growth was very rapid during the first half, "We don't expect it to be as good this year. However, while the second half was much slower, we don't expect it to be as bad this year. It should even out and turn out to be a little more of a normal year than the ups and downs of the past few years."

As for the outlook at Fay's Drug, Rhodes observes that "We are looking for a good year."

The supermarket industry, also selling necessities, in general shares his belief, basing its optimism on improved gross margins and on hoped-for labor concessions. ■

Chains still slashing prices to lower high inventories

Retailers are in a rut. Since Labor Day, they've been saying consumer confidence is high but the chains continue to slash prices to sell their slow-moving inventories.

Adversely affected by unseasonably warm weather in October, a softening of consumer demand and a desire to increase share of market, most chains offered price reductions on fall and winter merchandise as far back as Columbus Day.

This resulted in increased sales but a squeeze on gross margins and net earnings during the quarter which ended in either September or October.

(For most general merchandise retailers, the third fiscal quarter ends about Oct. 31. One major exception is R. H. Macy, which ended its fiscal first quarter on Oct. 27.)

As a result, there was a continuing escalation of price-cutting from the middle of the quarter through Christmas.

Survey of third quarter results shows an average sales gain of about 7.5% over the year-earlier quarter

An indication of the softening of consumer demand was the statement by Edward R. Telling, chairman and ceo, Sears, Roebuck, to the effect that revenues of Sears Merchandising Group reflected smaller gains in durable goods (in the third quarter) after two years of double digit increases in those lines.

Practically everyone said that they'd been slashing prices in an attempt to get rid of high inventories.

A survey of the financial results of 13 large general merchandise chains in the quarter ended in September or October taken by *Chain Store Age Executive* shows an average sales gain of about 7.5% over the year-earlier quarter. This excludes a 36% gain by Wal-Mart, which was an extreme.

Profits for the same chains, however, ranged all over the lot with K mart registering a 12.7% increase; J. C. Penney, 6.6%; May Department Stores, 12.2%, and Associated Dry Goods, 11.1%. But in the case of Penney, there is a footnote to the fact that LIFO (last-in, first-out method of inventory accounting) credits of $13 million were reflected in the quarter, compared with none in the comparable 1983 period.

Wal-Mart registered an impressive 38% increase in profits, Woolworth reported a 30% profit increase and Zayre had a 28.7% earnings increase. But Federated Department Stores had a 23.6% decrease, Dayton Hudson showed a 3% decrease, Macy reported a 26.9% decrease and Allied Stores, an 8.7% decrease.

May president David C. Farrell says all segments of his company's business improved in the third quarter in sales and earnings, compared with one of the strongest quarterly performances in the company's history.

Most chains offered price reductions on winter merchandise as far back as Columbus Day.

Sales and earnings for quarter ended in September or October

Chain	1984 sales (millions)	1983 sales (millions)	% change	1984 EPS	1983 EPS	% change
General Merchandise						
Sears[1]	$6,463	$6,190	4.4	—	—	—
K mart	4,993	4,331	15.3	$0.71	$0.63	12.7
Penney	3,211	2,914	10.2	1.34	1.26	6.6
Federated	2,266	2,071	9.4	0.87	1.14	(23.6)
Dayton Hudson	1,868	1,659	13.0	0.44	0.46	(3.0)
Woolworth	1,404	1,353	3.8	0.82	0.65	30.0
Wal-Mart	1,584	1,167	36.0	0.42	0.31	38.0
May	1,133	1,003	13.0	0.92	0.82	12.2
Macy	1,011	929	8.8	0.61	0.85	(26.9)
ADG	951	905	5.0	0.80	0.72	25.0
Allied	932	883	5.5	0.84	0.92	(8.7)
CHH[2]	906	758	20.0	0.05	0.15	(66.6)
Zayre	777	659	17.8	1.12	0.92	28.7
Supermarkets and convenience stores						
Safeway	4,584	4,300	6.6	0.65	0.82	(20.7)
Kroger	4,623	4,505	2.6	0.86	0.62	38.7
Southland	3,085	2,430	26.9	1.19	1.46	(18.5)
Lucky	2,191	2,027	8.1	0.30	0.35	(14.3)
Winn-Dixie	1,732	1,648	5.1	0.48	0.46	4.3
A&P[3]	1,377	1,192	15.5	0.31	0.20	55.0
Drug chains						
Walgreen	684	595	15.0	0.85	0.73	16.4
Jack Eckerd	637	543	17.3	0.35	0.30	16.7
Revco	511	453	12.6	0.42	0.44	(4.5)
Longs	328	291	12.7	0.79	0.72	9.7
Specialty stores						
Melville	1,066	985	8.2	0.68	0.71	(4.2)
Tandy	596	583	2.1	0.41	0.57	(28.0)
U.S. Shoe	416	375	10.9	0.46	0.85	(49.9)
Limited	349	271	29.0	0.47	0.35	34.0
Toys "R" Us	322	221	45.7	0.18	0.11	63.6
Edison[4]	269	249	7.8	0.88	0.96	(14.4)
Zale	217	198	9.6	0.04	—	—

( )decrease
[1]Sears Merchandise Group sales only. Operating profits from this group amounted to $163.8 million, or a 3.1% increase over the $158.9 million of a year earlier.
[2]Actual earnings increased 59%. Earnings per share declined because of actions taken by CHH to fight off a takeover attempt by Limited Inc.
[3]Before extraordinary credits in both years.
[4]Without a nonrecurring after-tax gain from the sale of Handyman Store properties in Texas and Oklahoma, earnings per share would have been 73¢ in the 1984 quarter, a 28.8% decrease.
Source: *Chain Store Age Executive*

For more information circle 44 on reply card.

"With the consumer in a positive frame of mind, and with two extra sales days between Thanksgiving and Christmas, we are optimistic about the outlook for the fourth [current] quarter."

Howard Goldfeder, Federated's chairman and ceo, says: "The third quarter was disappointing overall, although we see some positive indicators which should position Federated more favorably in the future."

He adds that the department and specialty stores and mass merchandising segments of Federated didn't perform as well as anticipated because of the warm weather, efforts to clear seasonal merchandise, strategies to enhance share of market and the "continuation of a highly promotional retail environment."

Bernard M. Fauber, K mart chairman, says the third quarter sales increases for his company reflected the impact of significant merchandising improvements completed in the quarter, in addition to the acquisitions of Waldenbooks and Home Centers of America.

He adds that additional borrowing was required as a result of the acquisitions and that this resulted in a 5¢-a-share reduction in earnings per share in the quarter.

Among major food chains, sales increases ranged from 2.6% for Kroger to a high of 26.9% for Southland, and included a 15.5% gain for The Great Atlantic & Pacific Tea Co. (A&P), 8.1% for Lucky, 6.6% for Safeway and 5.1% for Winn-Dixie.

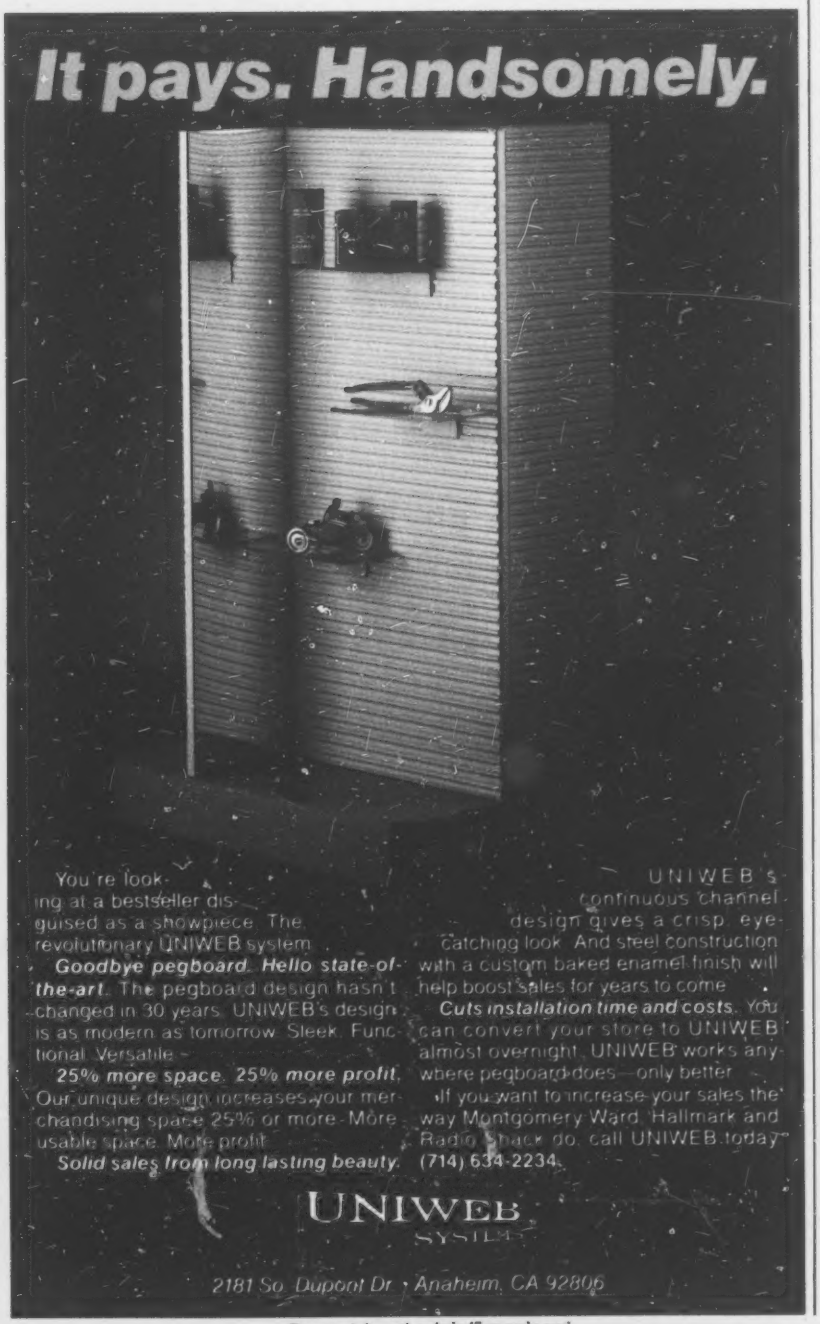
A rebounding A&P showed a whopping 55% earnings increase over the same year-earlier period, with Kroger reporting an impressive 38.7% increase. Safeway reported a 32.8% profit increase, Giant Food had a 10.3% increase and Winn-Dixie reported its earnings were up 4.3%. Southland, despite its huge sales increase, had an 18.2% decline in earnings with 16.1% more average shares outstanding, primarily due to its Citgo acquisition in August 1983. Lucky had a 14.3% decrease in profits; Giant, a 5% decline.

Kroger says net in the quarter included a $3.7 million, or 8¢ a share, from the retirement of some debentures. Kroger attributes the results to better retail performance and a cost-cutting campaign, which included a cutback of corporate staff by 12%. It also is closing stores in which employees won't grant wage and benefit concessions (*Chain Store Age Executive*, November 1984).

The drug chains showed a fairly consistent sales growth pattern of from 12% to 17%, but while Walgreens and Jack Eckerd showed profit increases in excess of 16% and Longs had a 9.7% increase, Revco reported a 4.5% decline.

In the specialty store field, Toys "R" Us led the way with a huge 45.7% sales increase and even more impressive 63.6% earnings jump. The Limited registered a 29% sales increase and 34% earnings improvement. Tandy (Radio Shack), U. S. Shoe and Edison Bros. all reported profit declines.

Toys "R" Us opened 34 stores, including four in Canada and one in Singapore, in 1984. It plans to add 40 to 50 stores this year, including its first unit in the United Kingdom. Toys "R" Us also opened eight Kids "R" Us children's clothing stores last year, bringing the total to 10. It plans to open 15 to 20 Kids "R" Us stores this year. ■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New centers pace industry upswing

Although the recovery began in 1984, this will be the year when the shopping center industry really takes off

The industry pundits have been predicting it and now the numbers are confirming that it is true. 1985 is shaping up as an extremely active year for the shopping center industry and the pace of development shows no signs of slackening.

Although 1984 signaled the beginning of the recovery, because of the long lead times characteristic of the industry it has taken until the current year for building to really take off.

Now a whopping 90% of developers queried plan to substantially increase total GLA before year-end, according to a survey conducted by *Chain Store Age Executive*. In addition, 80% of this group expects to achieve additional increases in 1986.

Such increases are particularly significant since they come on top of those additions to total GLA made last year by 70% of those surveyed.

This year a greater percentage of additions to GLA is expected to come from new construction, approximately 67%, compared to last year's 59%. Conversely, expansion of existing centers appears to have slowed somewhat, accounting for 20.7% of growth this year, down from 28.9%. Acquisition activity remains virtually unchanged at 12%.

The slowdown in center expansion seems logical since already these developers report having expanded 13.3% of their existing centers in 1984 and with the expansion of another 9.8% already on the drawing board for this year.

Looking ahead to 1986, those adding GLA expect 67% of the addition will be through new construction, while expansions will continue to decline as a percentage of total GLA additions, down to 18.6%. The rate of acquisitions is seen as quickening slightly to account for 14.9% of the GLA increase.

Of this year's survey respondents, 84% have some development responsibilities for neighborhood/convenience/community centers, also confirming another dominant trend in the industry. Forty-four per cent of the respondents cite such centers as

Development activity

	1984	1985	1986
Experienced/expect increase in total GLA:			
	70%	90%	80%
Among those experiencing increase:			
Level of increase in total GLA attained/expected (in sq. ft.)	680,000	616,000	792,000
Percentage of increase in total GLA resulting/expected to result from:			
New construction	59.1%	67.2%	67.0%
Expansion of existing centers	28.9%	20.7%	18.6%
Acquisition of centers	12.0%	12.1%	14.5%

Source: *Chain Store Age Executive* research

Types of shopping centers owned/managed

	Total	Primary area of involvement
Neighborhood/convenience/community centers	84%	44%
Regional malls	56	38
Mixed-use/multi-use centers in suburban locations	38	2
Mixed-use/multi-use centers in downtown locations	30	4
Off-price/outlet centers	30	6
Specialty centers	26	2

Source: *Chain Store Age Executive* research

Urban festival centers such as South Street Seaport illustrate the diversity of development.

Level of year-to-year increases in GLA

	1984 Primary area of involvement		1985 Primary area of involvement	
	Regional malls	Neighborhood/convenience/community centers	Regional malls	Neighborhood/convenience/community centers
100,000 sq. ft. or less	8%	19%	6%	10%
100,000-200,000 sq. ft.	17	31	6	16
200,001-400,000 sq. ft.	25	19	6	10
400,001-700,000 sq. ft.	8	6	29	16
700,001-1,000,000 sq. ft.	17	—	18	42
1,000,001-2,000,000 sq. ft.	17	19	29	16
2,000,001-4,000,000 sq. ft.	—	6	—	10
More than 4,000,000 sq. ft.	—	6	N.A.	N.A.
(Mean)*	(792)	(741)	(691)	(903)

*In thousands
N.A.—Not Available
Source: *Chain Store Age Executive* research

their primary type of retail real estate involvement.

Not surprisingly, the second most dominant area of involvement is regional malls with a majority of the survey respondents, or 56%, indicating that they own or manage such centers. It is the primary area of industry involvement for 38%.

When the survey respondents were questioned about their participation in other types of center development, the following results were obtained: mixed-use/multiuse centers in suburban locations, owned or managed by 38% of the group; mixed-use/multiuse centers in downtown locations, 30%; off-price/outlet centers, 30%, and specialty centers, 26%.

As for primary area of involvement, 6% cite off-price/outlet centers; 4% mixed-used/multiuse centers in downtown locations; 2% mixed-use/multiuse centers in suburban locations, and 2% specialty centers.

The current spurt of activity taking place in all these forms of retail development is a function not only of the general economic recovery, but also of the fortuitous convergence of a number of conditions unique to the shopping center business.

First, interest rates appear to be still on a downward trend *(see related story this issue)* and the availability of financing continues to improve (including a big influx of money into the industry from pension funds and other heretofore relatively untapped sources).

Second, in looking for ways to continue to grow their businesses, a number of the nation's department store companies have taken a now-or-never approach to entering new market areas and/or making stronger statements in existing ones. The result is that they are ready to commit to new mall projects.

At the same time, the boom in the specialty store business is providing developers with plenty of tenants to draw from both for mall space as well as in other locations. Existing chains are expanding, new ones are constantly emerging and even foreign operations are increasingly making their presence felt on the American scene. Witness, for example, the phenomenal growth of the Benetton chain, Laura Ashley's continuing quest for American sites, and now the entry of Canadian giant Dylex (*Chain Store Age Executive*, October 1984) as some examples.

Then, too, there is the emergence of new retail formats, including supermarket superstores and warehouse stores, deep discount drug operations, computer stores, discount book chains, megaoptical stores and, of course, off-price operators.

All this coupled with the continuing growth of such retail classifications as home centers and catalog showrooms (particularly Service Merchandise and Best Products) clearly shows where the tenants are coming from.

There's plenty of room for them, with this year's average increase in total GLA expected to be 616,000 sq. ft., according to the *Chain Store Age Executive* survey. This is down somewhat from the 680,000 sq. ft. reported for 1984. However, it's expected to jump all the way to 792,000 sq. ft. in 1986, reflecting the continuing swing back to new center construction.

Interestingly, a similar survey conducted by *Chain Store Age Executive* last year indicated that developers then expected to add only an average of 495,000 sq. ft. of GLA. One likely reason for the difference is that, finding themselves in an extremely favorable economic climate, developers quickly proceeded with such projects as strip centers, specialty centers and off-price centers, in particular, all requiring relatively short lead times.

At the same time, regional mall developers also took advantage of retailer interest and fast-growing markets to expand existing centers perhaps sooner than originally anticipated.

It now appears that for those involved primarily in neighborhood/convenience/community

Paying the price

Primary source of financing

	Total	Primary area of involvement: Regional malls	Primary area of involvement: Neighborhood/convenience/community centers
Open-end construction loan	28%	16%	32%
Conventional long-term mortgage	14	26	—
Internal financing	14	16	9
Revolving lines of credit	9	5	14
Insurance	8	10	9
Monies acquired through arrangements with pension funds	6	16	—
Syndication	6	—	14
IRBs	4	—	9
Permanent take-out	2	—	4
UDAGs	2	—	4
Public monies	2	—	—

Source: *Chain Store Age Executive* research

When it comes to the question of financing in the shopping center industry, the methods in use are as diverse as the types of shopping centers being developed, according to a recent survey undertaken by *Chain Store Age Executive*.

No one method is used as the main financing source by a majority of the respondents, although open-end construction loans continue to be the most prevalent. They are currently the primary source of financing for 28% of the respondents.

According to the survey, conventional long-term mortgages are being obtained by a lucky 14% of the respondents while 14% are relying primarily on internal financing sources. Revolving lines of credit are in primary use by 9% as are monies acquired from insurance companies.

Other primary methods of financing now in use include: syndication, 6%; industrial revenue bonds, 4%; permanent take-out loans, 2%; Urban Development Action Grants (UDAGs), 2%; and public monies (*i.e.*, bonds), 2%.

The survey also shows that the use of financing sources varies considerably according to the type of center under development.

Specifically, for those survey participants engaged primarily in regional mall construction, conventional mortgages lead all sources as the primary method of financing, at 26%, while open-end construction loans are the leader for neighborhood/convenience/community center builders, at 32%.

Conversely, open-end construction loans are the primary financing source for 16% of the regional mall developers, while conventional long-term mortgages are not the primary source for any of the neighborhood center builders.

Another source of financing heavily relied on by the mall builders but not at all by those involved in neighborhood center development is pension funds, cited by 16% of the mall group. Conversely, syndication is a primary source for 14% of the neighborhood center group, but not tapped into at all as a primary source for those involved in mall development.

Other financing methods utilized as primary sources by the neighborhood center developers and not at all by the mall developers include: industrial revenue bonds, permanent take-out loans and UDAGs. None of these are utilized as the primary source for the mall group.

centers, the trend toward new construction will accelerate this year. This group predicts that 72.1% of their 1985 increases in GLA will come from new center construction, up from 61.4% last year. Conversely, expansion of existing centers will fall to 20% from 26.8% of the total.

Acquisitions will play a lesser role as a means of adding GLA, falling to 7.9% from 11.8%.

However, new construction is also on the upswing for those involved primarily with regional malls. They are expecting that 54.1% of this year's addition to GLA will come from new centers, up considerably from 1984's 48.3% (a number obviously affected by the bleakness of the early part of the 1980's which took the bloom off regional mall plans). Correspondingly, expansion of existing centers is expected to slow considerably, accounting for only 27.9% of the growth in GLA, down from 40%.

In contrast to the situation with neighborhood centers, though, acquisitions are expected to play a more major role in contributing to mall GLA increases. Those involved chiefly in mall development expect acquisitions this year to contribute 17.9%, up from 11.7%.

The Arsenal Marketplace is an example of converting existing space into retail developments.

For those survey respondents planning to boost GLA before year-end, the anticipated average size of newly constructed centers averages 339,000 sq. ft.

As could be predicted, this is considerably higher for regional malls, at 557,000 sq. ft., than for neighborhood/convenience/community centers at 219,000 sq. ft. This also indicates that both malls and neighborhood centers are being downsized somewhat this year since in 1984 the average sizes were 521,000 sq. ft. and 104,000 sq. ft., respectively. The average for the total survey group was 228,000 sq. ft.

Yet, although the centers may be smaller, they may also be greater in numbers. While the survey shows the average number of new centers

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Average size (in GLA) of new 1984 centers

	Total	Primary area of involvement: Regional malls	Primary area of involvement: Neighborhood/ convenience/ community centers
Less than 100,000 sq. ft.	39%	14%	57%
100,000-250,000 sq. ft.	36	14	43
250,001-400,000 sq. ft.	11	14	—
400,001-700,000 sq. ft.	4	14	—
700,001-1,000,000 sq. ft.	11	43	—
(Mean)*	(228)	(521)	(104)

*In square feet
Source: *Chain Store Age Executive* research

Average size (in GLA) of 1985 centers

	Total	Primary area of involvement: Regional malls	Primary area of involvement: Neighborhood/ convenience/ community centers
Less than 100,000 sq. ft.	16%	—	28%
100,000-250,000 sq. ft.	40	18%	50
250,001-400,000 sq. ft.	21	27	17
400,001-700,000 sq. ft.	5	9	—
700,001-1,000,000 sq. ft.	16	46	—
(Mean)*	(339.0)	(557.0)	(219.0)

*In square feet
Source: *Chain Store Age Executive* research

opened per developer in 1984 was 2.8, this year it stands at 3.5.

Most of the increase comes from neighborhood center developers, upping their projects to an average 4.2 from 3.4, but the regional mall group has also boosted its plans to an average of 2.3 centers, up from 1984's 2.

While new center size may be on the decline, the size of expansion projects is on the upswing, according to the survey results. Of the respondents expanding existing centers this year, the average size of the project is 122,500 sq. ft., up from last year's average of 93,800 sq. ft. Expansions are obviously fewer in number, but bigger in size.

Somewhat surprisingly, the survey group reports that the cost per square foot for expanding centers, although having declined from last year's level, continues to be higher than that of constructing new centers, although this too has risen. The respondents estimate that it now costs $45 per square foot to expand existing properties, compared with $42.80 per square foot for new construction.

A further break-out shows a cost of $48.30 per square foot for regional mall expansion and $35 for neighborhood/convenience/community centers, compared with the costs of new construction of $46.90 and $39.80, respectively.

The same relationship existed last year when the costs per square foot for expansion projects were $43.30 per square foot, or $47.50 for regional malls and $41.70 for neighborhood/convenience/community centers, respectively.

These costs are all significantly more than the $38.30 reported for new construction, or $45.80 for regional mall construction and $36.70 for neighborhood center construction.

Geographically, the Southeast continues this year as the major area of development for the largest proportion of respondents. Approximately one-third of the developers planning additions to GLA, or 32%, are concentrating their construction activity in this region, down slightly from 39% in 1984.

Likewise, activity remains brisk in the Southwest, the area of concentration for 21% of those surveyed, the same level as last year.

However, this year will see an upsurge of activity in the Pacific and Midwest regions, cited by 18% and 13%, respectively, compared with 7% for each in 1984. The big loser is the Northeast, falling to 8% from 14%.

As for 1986, while the Southeast continues to be the most active area of development, otherwise it appears that building will be more evenly distributed throughout the various geographic regions. Specifically, 16% of the respondents identify the Midwest as their primary area of new construction, 16% the Southwest, 16% the Pacific region and 10% the mid-Atlantic region.

The shopping center industry is clearly on an upswing all over. ■